Landmark Judgments in Corporate Laws

(from the perspective of Corporate Secretarial compliance & Corporate Law Advisory)

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Scope & Coverage

- Scope of presentation – ‘Landmark’ & ‘Corporate Laws’– ?

- Scope of the landmark judgements
  - *Holding & Subsidiary Companies,*
  - *AoA vis-à-vis Shareholders Agreement,*
  - *Inspection of Book of Accounts & Statutory Registers*
  - *Meetings of Board of Directors,*
  - *Meetings of Shareholders,*
  - *Appointment & Rights of Directors.*

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Holding subsidiary relationship and capital gains tax exemptions to wholly owned subsidiary

CIT Vs Sunaero Ltd. [2012] 172 Comp Cas 562 (Delhi)

An exemption from capital gains tax in respect of transfer of assets by the subsidiary to the holding company was denied on the grounds that the subsidiary was not a subsidiary since some of its shares were held by individuals and they were not proved to be nominees of the Holding Co. holding the shares on its behalf

CIT Vs Sunaero Ltd. [2012] 172 Comp Cas 562 (Delhi)

- *Court pointed out that for availing of the benefit under section 47(v) of the Income Tax Act, 1961, the subsidiary must be a wholly-owned subsidiary of the holding company;*
- *Being a subsidiary is not sufficient. Thus, even if one of the shareholders was not a nominee of the holding company, the benefit under section 47(v) has to be denied.*
- *Court reiterated the principle that the normal presumption in law is that the registered shareholder holds the shares in his own right and in his individual personal capacity. He does not hold shares as a nominee of a third person;*
- *It is the contrary which has to be proved by the party who claims or asserts that the recorded shareholder is a nominee. The onus is on the party who claims to the contrary.*

Power to file a suit on behalf of Co. : Is the defect in authorization curable?

Sec.21 of Cos. Act, 2013:

Save as otherwise provided in this Act

(a) Document or proceeding requiring authentication by a company; or

(b) Contracts made by or on behalf of a company,

may be signed by any KMP or an Officer or employee of the Co. duly authorised by the BoD in this behalf.

State Bank of Travancore v. Kingston Computers (I) P. Ltd. [2011] 163 Comp Cas 37(SC)

- SC underscored the importance of proper authorisation in the case of litigation on behalf of a company in order to avoid the mishap of dismissal of the lawsuit at the entry level itself.

- SC called an improper document of authorisation *nothing but a scrap of paper* as no resolution was passed by BoD of the Co. delegating its powers to a director and to authorise someone else to file the suit on behalf of the company and a person who described himself as a director was authorised by the CEO of the company by a letter to file the suit.

Learnings from the SC Judgement

- Power to file the suit on behalf of the Co. must flow from BoD,
- BoD's delegation of the powers to director / officer of the Co. must contain the power to delegate by that director / xofficer to anyone else.

Inspection of Registers & Returns

Sec. 163(2) of Cos. Act, 1956

The registers, indexes, returns, and copies of certificates and other documents referred to in sub-section (1) shall, except when the register of members or debenture holders is closed under the provisions of this Act, be open during business hours (subject to such reasonable restrictions, as the company may impose, so that not less than two hours in each day are allowed for inspection) to the inspection—

a) Of any member or debenture holder, without fee; and
b) *Of any other person*, on payment of such sum as may be prescribed for each inspection.

Anilkumar Poddar Vs Futura Commercials (P.) Ltd. [2017] 136 CLA 1 (NCLT)

- *Petitioner who does not have any kind of interest in the Co. is not entitled to seek inspection of the records falling in ambit of Sec. 163. More so, when petitioner is a rank outsider, and Co. is Pvt. Ltd. Co. closely held by limited members.*

- *Words 'any other person' mentioned in Sec. 163 cannot be construed to mean that any person can seek inspection and supply of copies of the records falling in the ambit of Sec. 163. A person can be called aggrieved only when such person's interest is affected by the affairs of the company.*

Anilkumar Poddar Vs Futura Commercials (P.) Ltd. [2017] 136 CLA 1 (NCLT)

- *Word 'any other person' being preceded by the word 'member or debenture–holder' being the persons holding interest in a Co., the following word 'any other person' cannot be said that it is extendable to the persons having no interest in the Co.*
- *Apart from the member or debenture–holder, there being several other persons, having commercial interest in the company such as creditors, lenders, customers, employees, it can be said as referring to the category of persons mentioned above.*

Whether agreement between shareholders of a company binds the company?

V. B. Rangaraj Vs. V. B. Gopalakrishnan [1992] 73 Comp Cas 201

- Question before SC was *as to the enforceability of an agreement which was inconsistent with a private company's AoA was considered in context of transfer of shares.*

- Agreement between 2 groups of shareholders which imposed some restrictions on the transferability of shares held by them was not binding either on the Co. or its shareholders because the restrictions so imposed by the agreement were contrary to the provisions of the articles; a sale of shares held by one of the 2 groups in breach of the agreement could not, therefore, be held to be invalid.

V. B. Rangaraj Vs. V. B. Gopalakrishnan [1992] 73 Comp Cas 201

Private agreement which is relied upon by the plaintiffs where under there is a restriction on a living member to transfer his shareholding only to the branch or family to which he belongs in terms imposes two restrictions which are not stipulated in the article.

SC observed that:

Firstly, it imposes a restriction on a living member to transfer the share only to the existing members.

Secondly, the transfer has to be only to a member belonging to the same branch of family.

The agreement obviously, therefore, imposes additional restrictions on the members right to transfer his shares which are contrary to the provisions of Article 13. They are, therefore, not binding either on the shareholders or on the company.

Whether agreement between shareholders of a company binds the company?

Shanti Prasad Jain v. Kalinga Tubes Ltd. [1965] 35 Comp Cas 351 (SC)

- In this case, the shareholders of a Public Co. originally consisted mainly of 2 groups – A & B. Later on to meet the financial difficulties of the company, C agreed to supply finances on terms that he be allotted shares equal to those held by A and B group after increasing their share capital;

- Co. was not a party to the agreement. Nor were the AoA amended in order to incorporate the agreement;

- Later on the Co. converted itself into a public limited Co. in order to obtain advances from the Industrial Finance Corporation. At this time, though the AoA were amended, the agreement was not incorporated therein.

Shanti Prasad Jain v. Kalinga Tubes Ltd. [1965] 35 Comp Cas 351 (SC)

SC observed that:

- *The agreement between A, B, C did not mean that if in the future there was any increase in capital that will be shared equally by the 3.*

- *The Co., much less the public limited company when it was formed, not being a party to the agreement was not bound by it.*

Whether Comfort Letter is guarantee?

United Breweries (Holdings) Ltd. v. Karnataka State Industrial Investment & Development Corpn. Ltd. [2013] 176 Comp Cas 292 (Kar)

The contract of guarantee was a -contract to perform the promise or discharge the liability of a third person in case of his default.

The document did not reveal that the appellant had entered into a contract or an agreement with the Corporation to discharge the liability of the company in case of default.

Therefore, the appellant could not be made liable for more than it had undertaken. Admittedly, the Corporation had -insisted on the "letter of comfort" of the appellant while disbursing the loan in favour of the company and accordingly, the appellant being the holding company had given a letter of comfort as suggested by the Corporation.

Material on record, merely indicated the appellant's assurance that the -company would comply with the terms of a financial transaction without guaranteeing performance in the event of default. The order in so far as it fixed liability on the appellant was liable to be set aside.

Appointment of Directors

Sec. 196(3)(a) of Cos. Act, 2013

Extract of Relevant provision:

No co. shall appoint or continue the employment of any person as MD, WTD or Manager who:

(a) Is below the age of 21 years or has attained age of 70 years:

***Provided that** appointment of a person who has attained the age of 70 years may be made by passing a special resolution in which case the Explanatory Statement annexed to the notice for such motion shall indicate the justification for appointing such person.*

Schedule XIII, Part I, Clause (c) of Cos. Act, 1956

Extract of Relevant provision:

No person shall be eligible for appointment as MD, WTD or Manager of a Co. unless he satisfies the foll. conditions:

He has completed the age of 25 years and has not attained the age of 70 years:

Provided that where—

(*i*) he has not completed the age of 25 years, but has attained the age of majority; or

(*ii*) he has attained the age of 70 years; and

where his appointment is approved by a special resolution passed by the company in general meeting, no further approval of the CG shall be necessary for such appointment

Bombay HC: Director turning 70 years not to attract automatic 'mid-stream' disqualification

Sridhar Sundararajan ('SS')

Vs

Ultramarine & Pigments Ltd. &

Rangaswamy Sampath ('RS')

Broad Facts

- RS was appointed as CMD of listed co. on August 13, 1990. On May 21, 1998, SS was appointed as director.
- On August 1, 2012, RS was re-appointed as CMD for term of 5 years till 2017. On same day, SS was also appointed as Joint-MD.
- Cos. Act, 2013 was enforced w.e.f. April 1, 2014
- RS attained the age of 70 years on November 11, 2014.
- SS contended that "*On the 70th birthday of RS, he earned himself statutory disqualification*"

Interpretation of Single Judge

- *Sec. 196(3) does not operate to interrupt appointment of any Director made prior to coming into force of 2013 Act.*

- *It also does not interrupt the appointment of MD appointed after April 1, 2014 where at the date of MD's appointment / re-appointment was below the age of 70 years but crossed that age during his tenure.*

Contextual reading of the words in Sec. 196(3)

- Interprets Sec. 196(3), use of words "*No company shall appoint or continue the employment of….*", states that words should be read contextually.

- Draws parallel reference from Sec. 269 of 1956 Act, holds "*there was no 'discontinuance' of MD at the age of 70 years and the section applied only to his appointment (including re-appointment)*".

‘70 years’ was never an automatic mid-stream disqualification

- *70 years was never an automatic mid-stream disqualification even under 1956 Act.*

- Single Judge relied on SC ruling in P. Suseela & Ors. Vs University Grants Commission (2015) wherein it was held that “*it is relevant to distinguish between an existing right and vested right. Where a statute operates in future it cannot be said to be retrospective merely because within the sweep of it operation all existing rights are included*”

Bombay HC Division Bench: Automatic disqualification trigger for directors turning 70, though appointment made pre-Cos Act, 2013

Sridhar Sundararajan (‘SS’)

Vs

Ultramarine & Pigments Ltd. &

Rangaswamy Sampath (‘RS’)

"MD attaining 70 years would immediately be disqualified"

- Bombay HC's Single Judge Order was quashed.
- Division Bench held that disqualification for MD appointment on ground of age limit would act 'automatically'
- Thus, MD attaining 70 years would immediately be disqualified.
- *RS was disqualified from continuing as MD, unless he fulfilled the requirements of the proviso i.e. company has to continue his appointment by a special resolution and, secondly, that resolution must state the reason why the continuation is necessary.*
- *Intention was to change earlier position by providing that person who has been appointed as MD before he was 70 years old is prohibited from continuing as MD once he has attained the age of 70.*

"Language of Sec. 196(3)(a) is plain, simple & unambiguous"

- HC rejected RS's contention that Sec. 196(3)(a) is not applicable to MD's appointment before April 1,2014, held "*it would otherwise retrospectively affect vested right of such MD and, secondly, that there is presumption against legislation operating retrospectively*".

- *Language of Sec. 196(3)(a) is plain, simple and unambiguous and it applies to all MDs who have attained the age of 70 years and there is no distinction between MD who have been appointed before April 1, 2014 and those after April 1, 2014.*

- Div. Bench rejected reliance on MCA Circular that clarified conditions specified in Schedule XIII Part – I of Cos. Act, 1956 (requiring satisfaction only at the time of appointment).

Sec. 164 & 167 of Cos. Act, 2013

Sec. 164 – Disqualifications for director's appointment

Sec. 167 – Vacation of Office of director

Sec. 164(2) of Cos. Act, 2013

Disqualifications for director's appointment

No person who is or has been a director of a co. which:

(a) has not filed financial statements or annual returns for any continuous period of 3 FYs; or

(b) …..

shall be eligible to be re-appointed as a director of that company or appointed in other company for a period of 5 years from the date on which the said company fails to do so.

Sec. 167 of Cos. Act, 2013 – Vacation of Office of Director

Vacation of Office of director

(1) The office of a director shall become vacant in case:

(a) *He incurs any of the disqualifications specified in Sec. 164;*

(b) …

(c) …

(2) ….

(3) Where all the directors of a company vacate their offices under any of the disqualifications specified in sub-section (1), the promoter or, in his absence, the Central Govt. shall appoint the required number of directors who shall hold office till the directors are appointed by the company in the general meeting.

Kolkata CLB: Prospective application of Sec. 164 &167

Facts of the case

- Petitioners filed 397/398 petition alleging acts of oppression/mismanagement in affairs of Resp. Co.

- Petition was pending for adjudication;

- Respondents filed an application praying for an order of injunction restraining / declaring as non-est appointment of any Advocate-on-record / Counsels under claimed authorization of erstwhile directors of Respondent Co., as they had vacated their offices in terms of Sec. 167(1)

… Facts of the case

- Respondent Co. submitted that all erstwhile directors vacated their offices in terms of Sec. 167(1) read with Sec. 164(2), due to default committed by erstwhile directors in filing, the financial statements of Respondent Co. & and its subsidiary cos. for 3 consecutive years.

CLB: Prospective application of Sec. 164 & 167

- *Provisions of Sec. 164 & 167 have been notified w.e.f. April 1, 2014 and, hence, consequential action u/s 167(3) accrues on non-filing of financial statements for 3 years commencing from April 1, 2014.*

- *Erstwhile Directors continue to be validly and legally appointed directors and hence, the said Board of Directors is competent to appoint the Advocate by following the provisions of law.*

Alternate Director

Sec. 313 of Cos. Act, 1956: Alternate Director

- *BoD of a Co. may, if so authorised by its AoA or by a resolution passed by the company in general meeting, appoint an Alternate Director to act for a director ("Original Director") during his absence for a period of not less than 3 months from State in which meetings of Board are ordinarily held;*
- *Alternate Director appointed u/s 313(1) shall not hold office as such for a period longer than that permissible to Original Director in whose place he has been appointed and shall vacate office if and when the original director returns to the State in which meetings of the Board are ordinarily held.*
- *If the term of office of the Original Director is determined before he so returns to the State aforesaid, any provision for the automatic re-appointment of retiring directors in default of another appointment shall apply to the original, and not to the alternate director.*

Sec. 161(2) of Cos. Act, 2013 : Alternate Director

BoD of a Co. may, if so authorised by its AOA or by a resolution passed by Co. in general meeting, appoint a person, not being a person holding any alternate directorship for any other director in the Co., to act as an alternate director for a director during his absence for a period of not less than 3 months from India:

***Provided** that no person shall be appointed as an alternate director for an ID unless he is qualified to be appointed as an ID under the provisions of this Act:*

***Provided further** that an alternate director shall not hold office for a period longer than that permissible to the director in whose place he has been appointed and shall vacate the office if and when the director in whose place he has been appointed returns to India:*

***Provided also** that if the term of office of the original director is determined before he so returns to India, any provision for the automatic re-appointment of retiring directors in default of another appointment shall apply to the original, and not to the alternate director.*

Bombay HC: Decodes 'Alternate Director', weighs on intention & permanence, not flying visits & vacations

Presence of Alternate Director at the time of appointment

- *For Alternate Director to cease to be a Director, the actual attendance at Board Meeting of the Director appointing him is not contemplated u/s 313 of Cos. Act, 1956;*
- *Consequently, the return to the State would suffice though the Director does not commence attending Board Meetings held after his return.*

HC interprets 'return to the State' – Length of time & intention is important

- *If a Director merely comes to the State and leaves India again he would not be able to transact business. Hence, Alternate Director would require to continue until the Director appointing him would have continued.*
- *What precisely the Section contemplates by the term "Original Director returns to the State", must be read as contemplating only such return which would have some amount of permanence.*
- *Director must return to carry on the business. He must return for a length of time. The intent of the Director must be not to make his visit merely temporary when he does not partake in the management of Co. and when he intends to go abroad again.*

HC: "Intention to return to India… Not for holiday or on vacation"

- *It should therefore, be the intention to return to India and the State in which the Board Meetings are ordinarily held (i.e., where the registered office is generally situate) not for a temporary period e.g., on a holiday or on vacation. It will imply the intention akin to the intention required to be domiciled in the State.*
- *Therefore, when original Director returned to India and the State in which the BMs were held to carry on his business in India that the Alternate Director would vacate his office u/s 313(2) of Cos. Act, 1956.*

Concept of ‘Compulsory Resignation’

Compulsory Resignation

Vs.

Removal of Director

Sec. 164 – Disqualification of Directors

Sec. 164(3) of Cos. Act, 2013: A private company may by its AoA provide for disqualifications for appointment as a director in addition to those specified in Section 164(1) and (2).

Can a company provide in its AoA as follows:

"Office of a director shall be become vacant if he be requested in writing by all his co-directors to resign."

MCA Circular (dated August 17, 1963) stated:

"Private Co. which is not a subsidiary of public co. cannot circumvent the provisions of Sec. 284 of the Act in the guise of including additional grounds in its AoA for vacation of office by directors, the power can be exercised by the Co. in general meeting as contemplated u/s 284 of Cos. Act"

Privy Council in Lee Vs Chou Wen Hsien (1985) BCLC 45: (1984) 1BCC 99, 291 (PC)

Although the power of expulsion vested in the directors was a fiduciary power and accordingly in exercising it they had to act in what they believed to be the best interests of the company and not for ulterior purposes, the expulsion provisions in the Co.'s AoA was so drafted as to require a director to vacate immediately his office once he had been requested to do so by the other directors.

Even if one or more of the requesting directors acted from ulterior motives the expulsion would be effective, provided the stated events for a valid expulsion had been satisfied.

Can permanent director be removed from the Co.?

Tenure of:

MD,

WTD,

Manager,

ID,

Non-ID.

- **No provision in Co. Law.**
- **Can Co. appoint a director as 'permanent director'?**
- **Can such director be removed by Co.**

Tarlok Chand Khanna Vs Raj Kumar Kapoor [1983] 54 Comp. Cas. 12 (Delhi)

- *Co. has power u/s 284 of the 1956 Act to remove a permanent director even if AoA put restriction on removal of Permanent Director;*

- *Even where in terms of AoA - Permanent Director was to hold office for life and also had a right during his life time to nominate his successor on the board in event of his death, that director could nevertheless be removed u/s 284 of 1956 Act.*

Duties of Directors

Sec. 166 of Companies Act, 2013

- *Subject to the provisions of Cos. Act, a director shall act in accordance with the Articles of Co.*
- *Director shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.*
- *Director shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment.*
- *Director shall not involve in a situation in which he may have a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the company.*
- *Director shall not achieve or attempt to achieve any undue gain or advantage either to himself or to his relatives , partners, or associates and if such director is found guilty of making any undue gain, he shall be liable to pay an amount equal to that gain to the company.*
- *Director shall not assign his office and any assignment so made shall be void.*
- *If a Director of the company contravenes the provisions of this section such director shall be punishable with fine which shall not be less than Rs. 1 lac but which may extend to Rs. 5 lacs.*

Delhi HC: Director carrying competing business breaches fiduciary duty, imposes restriction, interprets Sec. 166

Rajeev Saumitra

Vs

Neetu Singh

Facts : Director commencing competing business

- Plaintiff ('Husband') & Defendant (wife) were holding 50% shares in Paramount Coaching Centre Pvt. Ltd. (earlier, sole proprietary) Co. was in the business of imparting education, training for various national competitive examinations;
- Wife had approached Plaintiff to allow her to teach English subject in the coaching institute;
- Wife had poor financial condition. After 8-9 months, parties got married.

… Facts : Director commencing competing business

- After marriage, wife started hatching conspiracy to get her family members inducted in Co. and accordingly with necessary consents / permissions were taken for conversion of Coaching Centre into Co.

- Simultaneously, wife incorporated OPC ('Paramount Reader Publication Pvt. Ltd.') and started competing with the business of Paramount Coaching Centre Pvt. Ltd. i.e. diverting the business, staff, students and monies.

- Parties disputed on TM – 'PARAMOUNT' & approached Civil Court.

- Husband filed petition u/s 397-398 for mismanagement in Paramount Coaching Centre Pvt. Ltd.

HC: Director carrying competing business breaches 'fiduciary duty'

- HC held that wife has breached fiduciary duty u/s 166 of Cos. Act, 2013 by initiating competing business;
- Restrained her from using TM of 'Paramount'
- *"She has not exercised her duty with due & reasonable care, diligence & she was involved in the situation in which there was a direct interest that conflicted with co.'s interest, in order to gain advantage by herself and her relatives….. Being a Director, wife is guilty of making undue gain and she is also guilty of carrying out competing business of co."*

HC: Sec. 166 stipulates 'Duties of a Director to a Co.' and not 'Rights of Shareholders'

- *In case a Director violates the duties prescribed in Sec. 166, the cause of action accrues in favour of Co.;*
- *Sec. 166 is akin to the common law right. It is merely repository to Director's fiduciary duties, it does not apply to the shareholder;*
- *Even if his/her co. may or may not be benefitted from the same, the said party is under a duty to pay over to co. which he or she has betrayed by disloyalty.*

Wife has failed to cross the hurdle of mandatory provision of Sec. 166 – Husband has filed solid evidence

- *Defendant No.1 in the instant case has failed to cross the hurdle of the mandatory provision of Sec. 166 (which is incorporated in April 2014) in Cos. Act, 2013;*
- *The plaintiff has filed solid evidence which is unimpeachable, thus common remedy is available to the plaintiff against the act of defendant No.1;*

Sec. 88 of Indian Trust Act: Advantage gained by fiduciary

- *Where a Trustee, Executor, Partner, Agent, Director of a Company, Legal Advisor, or other person bound in a fiduciary character to protect the interests of another person, by availing himself of his character,*
- *Gains for himself any pecuniary advantage, or where any person so bound enters into any dealings under circumstances in which his own interests are, or may be, adverse to those of such other person and thereby gains for himself a pecuniary advantage,*
- *he must hold for the benefit of such other person the advantage so gained.*

Section 16 of Partnership Act: Personal profits earned by partners

Subject to contract between the partners:

(a) *<u>If a partner derives any profit for himself from any transaction of the firm</u>, or from the use of the property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm;*

(b) *<u>If a partner carries on any business of the same nature as and competing with that of the firm</u>, he shall account for and pay to the firm all profits made by him in that business.*

Liability of Directors

Section 149(12) of Cos. Act, 2013

Notwithstanding anything contained in this Act:

1. *Independent Director;*
2. *NED not being promoter or KMP,*

shall be held liable, only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable through Board processes, and with his consent or connivance or where he had not acted diligently.

Sec. 179 of Income Tax, 1961

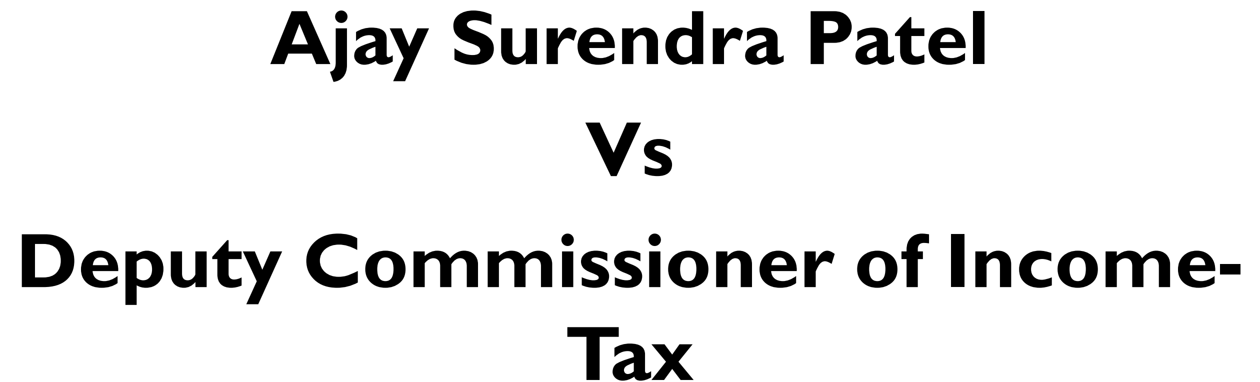
Sec. 179 of Income Tax, 1961

Liability of directors of private company in liquidation

Notwithstanding anything contained in the Cos. Act, 1956, where any tax due from Private Co. cannot be recovered, then, every person who was a director of Private Co. at any time shall be jointly and severally liable for the payment of such tax

Unless he proves that non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of Co.

Guj. HC: Pierces corporate-veil, Holds director liable for tax-dues of 'de facto' Pvt. Co.



Broad Facts:

- Petitioner was appointed as Additional director of Hirak Biotech Ltd. ('HBL') and was holding 98.33% of the shareholding in HBL.
- Income Tax Dept. raised demand for Rs. 240.82 lakhs on account of tax evasion which pertained to the year during which petitioner was acting as a director.
- Dept. initiated recovery proceedings and made all possible efforts to recover impugned demand. It was then contended that substantial accommodation entries were made during the period when petitioner was director in HBL.
- Dept. holding that HBL was set-up essentially for accommodation entries, invoked Sec. 179 of Income Tax Act.
- Petitioner-Director filed a writ petition before Gujarat HC.

Facts leading to lifting of Corporate Veil

- Existence of huge financial transactions, serious default, total non-co-operation in Co.
- HC observed that Co. appears to have been spearheaded by one of the directors only.
- Serious defaults in financial transactions with J&K Bank & Ahmedabad People's Co-Op. Bank of huge amounts
- HC observed that *"all these combination of circumstances makes this is a fit case to resort to a principle of lifting of corporate veil enshrined in Sec. 179 of Income Tax Act".*

HC's observation w.r.t. "Accommodation entries"

Main Object of the Co. was to carry on the business of floriculture, agriculture, horticulture etc.

However, the Co. had executed its business that of trading and distribution of ice-cream quite de-hors from the main object

HC observed that "*It appears that Co. is set-up for different purpose than which is posed before the authority at the time of incorporation. Therefore, the inference which has been raised by Dept. that Co. is set up essentially for the purpose of accommodation entries might not be ignored, though attempt is made to establish contrary.*"

History of Petitioners Background

- Petitioner has resigned in Sep. within a short span
- But, thereafter there was no substantial business of Co.
- After that there is huge accrual of debts of Co.
- And for recovery of that, even the properties have been auctioned and sold away under the steps of Securitization Act and
- ***Therefore, it appears that after resignation of the petitioner what has been left with the company is huge liabilities only***.
- Huge demand to the extent of Rs. 240.82 lacs of Tax Revenue remained outstanding and despite aforesaid vigorous steps, nothing is recovered from Co. which has compelled the Dept. to initiate action u/s 179 of Income Tax Act against all the responsible directors.

Factual matrix – Director's gross neglect – Income Tax provisions invoked by HC

- *Entire factual matrix would clearly indicate that this position of Co. in a gradual process to a virtual closure is on account of gross neglect, misfeasance or beach of duty on the part of directors in relation to Co. affairs.*

- *Therefore, the conditions which are contained in Section 179 before its invocation are appearing on the face of it which rightly visualized by the Dept. for passing the order which is impugned in the petition.*

Director's duties u/s 166 vis-a-vis Corporate Governance

- Fiduciary obligation does not cease with Resignation.
- Sec.166(3) of Cos. Act which spells out that director shall exercise his duties with due and reasonable care.
- HC relied on SC's ruling in N. Narayanan v. Adjudicating Officer, SEBI [AIR 2013 SC 3191], wherein it was held that "*Failure of Corporate Governance on the part of directors if they failed to exercised due care and diligence and thereby, allowing fabrication of figures and false disclosure, they would be liable for such omissions and commissions*".

Public Co. considered as 'Private Co.' for Sec. 179 of Income Tax Act

- *Close look at Co. affairs, the manner in which affairs proceeded with, all indicate that in actual terms Co. has not acted as Public Ltd. Co. in true sense;*
- *During tenure of petitioner, huge cash flow is deposited and practically use of cash flow deposit to be looked into substantially the Co. is used for object for which it has not been set-up;*
- *No involvement of public in Share Capital or in any form of asset and there is no share subscription issued from public by Co. in question;*
- *Therefore, practically the Co. appears to have systematically operated as if it is a private concern. On the contrary, Public Limited Co. has to act more in responsible manner than Private Ltd. Co.*

Board Meetings

At board meeting – Can one director constitute quorum

Relevant Provisions of Cos. Act, 2013

- **Sec. 167(3):** Where all the directors of a Co. vacate their offices under any of the disqualifications specified in sub-section (1) of Sec. 167, the promoter or, in his absence, the Central Govt. shall appoint the required number of directors who shall hold office till the directors are appointed by Co. in the general meeting.

- **Sec. 174(1):** Quorum for a meeting of the Board of Directors of a company shall be 1/3rd of its total strength or 2 directors, whichever is higher, and the participation of the directors by video conferencing or by other audio visual means shall also be counted for the purposes of quorum.

- **Sec. 174(2):** Continuing directors may act notwithstanding any vacancy in the Board; but, if and so long as their number is reduced below the quorum fixed by the Act for a meeting of the Board, the continuing directors or director may act for the purpose of increasing the number of directors to that fixed for the quorum, or of summoning a general meeting of the Co. and for no other purpose.

Pradip Kumar Banerjee Vs UoI [2002] 108 Comp Cas 692(Cal)

- AoA fixed maximum number of directors at 15, but there were only 6 directors actually holding the office when the dispute arose and it was argued that at a meeting of the Board at that point of time there was no requisite quorum as there were only two directors present. AoA provided that the quorum for board meetings shall be 1/3rd of the total strength of BoD

- Calcutta HC held that the meeting had requisite quorum.

K. C. Pandalai v. South Indian General Assurance Co. Ltd. [1941] 11 Comp Cas 327 (Mad)

- Resolution passed at a meeting where Quorum is not available due to presence of an interested director is invalid;

- *Where a resolution to set off an amount out of the amount due to a director by the Co. against what he owed in respect of shares allotted to him, was passed at a board meeting where 2 of 3 directors were brothers and therefore interested in the resolution, so that excluding the presence of these 2 directors there was only 1 director present resulting into inadequate number to constitute a quorum.*

- Court held that, the resolution was invalid.

NCLT: Quashes Board resolutions passed without Joint MD participation, despite availability on 'Skype'

Rupak Gupta

Vs

U.P. Hotels Ltd.

Cos. (Meetings of Board & its Powers) Rules, 2014

Rule – 3

Cos. (Meetings of Board and its Powers) Rules, 2014

(Meetings of Board through video conferencing or other audio visual means)

Rule 3(3): Co. shall comply with foll. procedure, for convening & conducting BMs through video-conferencing or other audio visual means.

Rule 3(3)(e): Director, who desire, to participate may intimate his intention of participation through the electronic mode at beginning of calendar year and such declaration shall be valid for one calendar year.

Obligation upon directors convening the meeting to provide every facility to directors asking video conference

- *Rule 3 is meant for providing video-conferencing, indeed it is the duty of directors convening the Board meeting to inform other directors regarding the options available to them to participate in video-conferencing mode or other audio video mode or other options available to them.*

- *It is the obligation upon directors convening the meeting to provide every facility to directors asking video conference and enable them to participate in Board meeting.*

NCLT's observations on Board Meeting via video-conferencing

- ***"Sub-rule 3(e) only says that if intimation is given at beginning of Calendar Year that will remain valid for entire Calendar Year. It is not said anywhere that if it is not given at beginning of year, Video Conference facility is not to be provided in that Calendar Year.***
- ***It does not mean that directors are not entitled for Video Conferencing if intimation is not given at beginning of Calendar Year.***
- ***When a provision is read, it has to be read wholly and not in pieces"***

Participation in board meeting through video conferencing – Whether right of a director or subject to availability of facility by company?

Achintya Kumar Barua alias Manju Baruah Vs Ranjit Barthkur [2018] 91 taxmann.com 123 (NCLAT)

- *Section 173(2) of the Act gives right to a director to participate in the meeting through video-conferencing or other audio-visual means and the Central Govt. has notified Rules to enforce this right and it would be in the interest of the companies to comply with the provisions in public interest;*
- *Coming to the facts of the present matter, it can be seen that NCLT took note of the fact that the company in this matter had all the necessary infrastructure available.*
- *NCLT came to the conclusion that the provisions of section 173(2) of the 2013 Act are mandatory and the companies not be permitted to make any deviations therefrom;*
- *NCLT's order could not be interfered. NCLT order must be said to be progressive in the right direction and there is no reason to interfere with the same.*

General Meetings

Notice of Meeting: Accidental omission to give notice or non-receipt of notice would not invalidate the proceedings at a general meeting

Sadhan Kumar Ghosh Vs Bengal Brick Field Owner's Association [2011] 163 Comp Cas 493

- *Plaintiff had not been able to demonstrate that those in control of the company management had deliberately failed to issue notice of the EGM to the plaintiff;*

- *Certificate of Posting produced by the defendants carried a stamp of postal authority and prima-facie established dispatch of notice;*

- *The amendments approved by the members in the meeting had been approved by the Central Govt. as required for companies governed by Section 25 of 1956 Act;*

- *The injunction seeking to set-aside the amendment of the MoA and AoA was to be declined. "Accidental omission to give notice or non-receipt of notice would not invalidate the proceedings at a general meeting."*

Proxy for attending general meeting – is it mandatory to appoint a proxy by proxy form only?

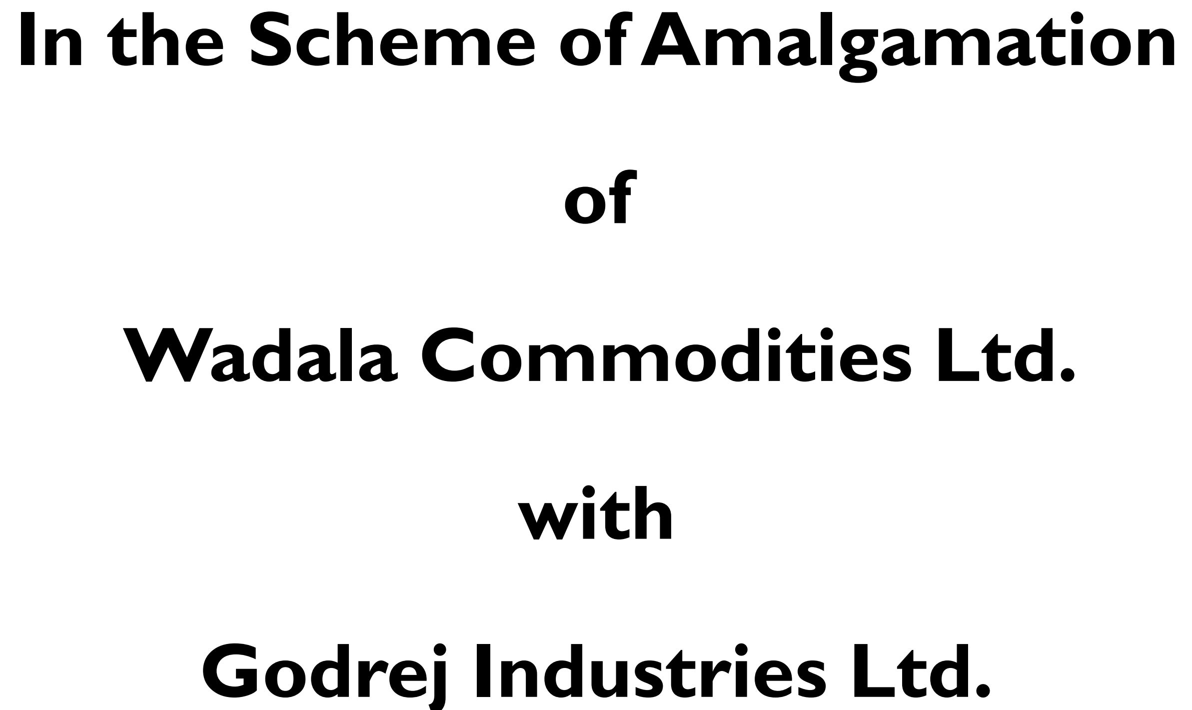
Gharda Chemicals Vs Jer Rutton Kavasmaneck [2006] 129 Comp Cas. 642 (Bom.)

- *It is however not mandatory to appoint a proxy only through the Form in Schedule IX;*
- *Even though Schedule IX to Act sets-out form of proxy, it may be varied if circumstances so require;*
- *So long as any instrument contains all the requisite particulars set-out in the Form in Schedule IX, it can be treated a proxy.*

Gharda Chemicals Vs Jer Rutton Kavasmaneck [2006] 129 Comp Cas. 642 (Bom.)

- *If an instrument contains all the requisite particulars such as name of Co., name of the person executing the instrument, name of the person empowered to vote as the proxy, etc., as set out in the Form in Schedule IX to the Act then such an instrument can be treated a proxy, e.g. Power of Attorney.*

Bombay HC: Compulsory voting by postal ballot/e-voting not applicable to Court-convened meetings



Postal Ballot

Extract

of

Sec. 110

of

Cos. Act, 2013

(1) Notwithstanding anything contained in this Act, a company:

*(a) **shall**, in respect of such items of business as the Central Government may, by notification, declare to be transacted only by means of postal ballot; and*

*(b) **may**, in respect of any item of business, other than ordinary business and any business in respect of which directors or auditors have a right to be heard at any meeting, transact by means of postal ballot,*

in such manner as may be prescribed, instead of transacting such business at a general meeting.

(2) If a resolution is assented to by the requisite majority of the shareholders by means of postal ballot, it shall be deemed to have been duly passed at a general meeting convened in that behalf.

Whether in view of Sec. 110 of Cos. Act, 2013 and SEBI Circular (May 21, 2013), a resolution for approval of Scheme of Amalgamation can be passed by majority of equity shareholders casting their votes by Postal Ballot (which includes e-voting) in complete substitution of an actual meeting?

Justice GS Patel's incisive commentary

- *Heart of Corp. Governance lies transparency and well-established principle of indoor democracy that gives shareholders qualified, yet definite and vital rights in matters relating to company functioning in which they hold equity.*
- *Principal among these, is not merely right to vote on any particular item of business, so much as the right to use vote as an expression of an informed decision. Therefore,* ***Shareholder has an inalienable right to ask questions, seek clarifications and receive responses before he decides which way he will vote****.*
- *Schemes of Arrangement/Compromise are amended at a meeting itself. These amendments come from the floor or even perhaps from Board itself. Amendment is then put to vote.*
- *In a postal ballot, no such amendment is possible.* ***If we were to restrict ourselves to a postal ballot, no shareholder or any director could ever suggest any amendment. Scheme would stand or fall only in its original form. This is contrary to the mandate of Sec. 391-394.***

‘Called’ Meeting V/s ‘Ordered’ Meeting

- *Even so Sec. 230 still speaks of ‘**calling of a meeting**’ and ‘**not merely putting the matter to vote**’. It has to be remembered that all schemes that are put to meeting of shareholders are proposed schemes. This means that they are subject not only to approval by voting but also, possibly, to an amendment at the meeting itself.*

- ***Meetings for approval of Schemes u/s 391/394 of 1956 Act are not ‘called’ by Co. Such meetings are ‘ordered’ by the Court.***

Dialogue & discourse are fundamental to making of every such informed decision

- *Nothing could be more detrimental to shareholders' rights than stripping them of the right to question, the right to debate, the right to seek clarification; and, above all, the right to choose, and to choose wisely.*

- *Vote is an expression of Opinion & it must reflect an informed decision. Dialogue & discourse are fundamental to making of every such decision.*

Conclusion

- ***Provisions for compulsory voting by postal ballot & by e-voting to exclusion of actual meeting cannot & do not apply to 'court-convened meetings'***

- ***At Court convened meetings, provision must be made for postal ballots & e-voting, in addition to an actual meeting.***

- ***Elimination of all shareholder participation at an actual meeting is anathema to some of the most vital of shareholders' rights,***

- ***It is strongly recommended that till this issue is fully heard and decided, no authority or any company should insist upon such postal-ballot-only meeting to the exclusion of an actual meeting.***

- ***Govt. & SEBI should appear before Court, when this matter is next taken up for a consideration of this issue.***

Q & A Session

Thank you ICSI WIRC for the wonderful opportunity!! ☺

Thank you Members for active participation! ☺

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